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FINANCE AND AUDIT SUBCOMMITTEE MEETING MINUTES

January 12, 2016

**California Department of Health Care Services Building
1500 Capitol Avenue
Sacramento, CA 95814**

The Finance and Audit Subcommittee of the California High-Speed Rail Authority (Authority) Board met on January 12, 2016 at 8:30am in the California Department of Health Care Services Building.

Committee Board Members Present:

Mr. Michael Rossi, Chair
Mr. Tom Richards

Board Members Present:

Ms. Thea Selby
Mr. Lou Correa

Authority Staff Present:

Mr. Jeff Morales, CEO
Mr. Dennis Trujillo, Chief Deputy
Mr. Tom Fellenz, Chief Counsel
Mr. Russell Fong, CFO
Mr. Jon Tapping, Director of Risk Management and Project Controls
Mr. Scott Jarvis, Chief Engineer
Ms. Paula Rivera, Chief Auditor
Ms. Deborah Harper, Chief Administrative Officer
Mr. Alan Glen, Director of Real Property
Mr. Mark McLoughlin, Director of Environmental Services
Mr. Terry Ogle, Director of Design and Construction
Mr. Paul Engstrom, Third Party Manager

Rail Delivery Partner Staff Present:

Mr. Gary Griggs, Rail Delivery Partner Program Director

Minutes prepared in the order items were presented during the meeting

Agenda Item – December 2015 Meeting Minutes

- No comments.

Agenda Item – Action Items from Previous Finance and Audit Committee Meeting

- None.

Agenda Item - Financial Reports – Russell Fong

Questions asked and answered. Issues discussed included:

- **Capital Outlay Report** – Mr. Rossi asked about the Central Region being over budget, why it is over budget and who approves this being over budget. Mr. Fong replied that in the current process the authorization would have to come from the Finance and Audit Committee. Mr. Richards asked if the Finance and Audit Committee was in operation at the time this went over budget, and Mr. Fong replied yes but this was back in 2014. During that time we did not highlight the budget at the segment level. For the current process we highlight all issues at the segment level. Mr. Richards asked for the answer to his question next month, a more detailed answer including what the procedure is, how it happens without it coming here, and what's the process before it gets here. Mr. Rossi asked if there is anything in play at this stage that will lead us to being over budget on any line items. Mr. Fong replied if you look at the Capital Outlay Report, page 3 of 9, there are some hot spots. Mr. Rossi asked what's the process to ensure we don't go over budget before it's properly approved. Mr. Fong replied that in the current process, budget shifts go to the Finance and Audit Committee. The Change Control Committee will identify those overages. Mr. Jarvis added that we are moving from being a planning organization toward more of a project management organization with project managers. The project managers will be the single focal point for scope, cost and schedule for the projects. Part of that will be monitoring the various tasks including the environmental clearance tasks and the budget for those tasks. We are developing work plans for each of our projects which will clearly delineate the tasks needed to deliver the projects and the budget for each of those tasks. Moving forward we will be more proactive as far as determining if any of those tasks are going over budget based on an earned value analysis including the environmental tasks. Mr. Rossi added that budget overages are not to happen without the appropriate approval.
- **Contracts and Expenditures Report** – Mr. Richards asked if all of the contracts are included in the budget. Mr. Fong replied that is correct. Mr. Richards asked for when the contracts are executed, for the expiration dates and what the forecast expenditures are in each current fiscal year. How are we planning for cash flow requirements? How are we managing these contracts? When you come over to the contract expenditure side, is it just the assumption? The AECOM + DMJM Altamont Corridor contract looks like expenditures on a \$55 million contract are only going to be \$10.3 million. Does that mean the contract is going to be amended to make provision for if it's only a \$10.3 million contract? Mr. Fong replied that we will need to follow up with the contract manager on that. Mr. Richards asked when we see no activity, why don't we eliminate the contracts. The new information, when provided, will help us see how these contracts are being managed. Mr. Fong replied that on a monthly basis we do contact the contract managers to see if the contracts need to be terminated. If the contracts are on the report with no activity, there is a reason. Mr. Richards asked why on the AECOM + DMJM Altamont Corridor contract forecasted expenditures (thru contract term) are only \$10.3 million on a \$55 million contract. Mr. Morales replied that the expenditure forecast is not accurate, it is the amount that has been spent. On that contract the Board approved transfer of that contract to the Altamont Corridor Express (ACE). Mr. Richards replied that it is not clear. Where it says forecasted you'd assume it is forecasting to the future. Mr. Rossi commented that if the actual expenditures equals the forecasted expenditures (thru contract term), the contract is dead. Mr. Richards asked if that is correct. Mr. Fong replied that he would need to follow up on it.
- **Operations Report** – Mr. Rossi commented that the executive summary has become too long. Mr. Rossi commented that ROW looks like it will be better than the alternative forecast, even when accounting for the public sector parcels. Staff is to be congratulated. CP 2-3 looks better. Mr. Glen added that the Operations Report only includes data thru November, 2015. In December we delivered 34 additional parcels in CP1 and 17 additional parcels in CP 2-3. Mr. Rossi asked what is the makeup of the 34 parcels. Mr. Glen replied that all were private parcels except for 9 Union Pacific parcels. 2015

to date we delivered 322 in CP1, 142 in CP 2-3 for a total of 464 parcels. As with CP 1, public parcels will be added in at a later date. Mr. Rossi asked if we are on the trajectory to spend the ARRA funds. Mr. Tapping replied that the current ROW delivery and capital expenditure projections, when overlaid with the current risk analysis, indicates that ARRA funds will be expended provided that ROW continues to deliver above the alternative forecast currently specified in the Operations Report.

Mr. Rossi asked for updates on environmental. Mr. McLoughlin replied that the Environmental Milestones Schedule (to ROD), page 31, has updates. A column was added that shows the original compared to the revised target dates of the EIR/EIS to be completed. We are still on target for 17 of the dates. The biggest change was the Wye from Dec-16 to Oct-17. Descriptions of the status of the different segments have been added on page 32. The forecast data requested on the Bakersfield F Street Station Alignment, page 38, is not updated yet but will be ready by the next meeting. Mr. Fong added the Environmental team went from 4 charts last month to 8 charts with a forecast. Mr. Rossi asked if the budget is ok. Mr. McLoughlin replied at this time yes. Mr. Rossi asked for more of an explanation. Mr. McLoughlin added if unanticipated things occur, the stakeholder input on the preferred alternatives, how we arrive at those, how we get consensus of those, how much time that takes can change the way that we are doing the project to get to that consensus preferred alternative. Mr. Rossi asked whether or not, with the probabilities as they stand, that we have the necessary budget for these exercise. Mr. Tapping responded that the Authority is currently implementing a schedule/cost risk analysis an all environmental segments. Mr. Rossi asked when we will be able to see that. Mr. Tapping estimated that preliminary results would be complete in a month and a half. Mr. McLoughlin added that from an environmental aspect, we have a strong focus on project and program management for each of the sections coordinating with RDP project managers and their engineering counterparts. Mr. Rossi asked Mr. McLoughlin if there is anything he's worried about. Mr. McLoughlin replied that the size and magnitude of the sections to get RODs and permits to enable construction. Mr. Rossi asked if the parcel configurations for CP1 thru CP4 are sufficient to make sure we don't have holdups for construction. Mr. Jarvis replied that we are getting to a point that we have critical mass to start construction at multiple locations with ROW. The design and construction team work very closely with the ROW team to strategically focus on the parcels we need the most. We are at a point that ROW is not holding up construction at multiple locations thru that exercise. We look at the gross numbers which is important but probably even more important is the strategic parcels. Mr. Rossi asked if Mr. Jarvis is comfortable we have those. Mr. Jarvis replied that he is comfortable that we have ROW at multiple locations to start construction. We need to continue to focus on the right parcels. Mr. Morales added that all of the priority parcels that we identified jointly with the contractor are not an issue. Mr. Richards asked as we look past those priority parcels if we have a listing of the next tier of jobs, job sites, and where we are on those ROW acquisitions. Mr. Jarvis replied that we transferred into that phase. We have been working with the design builder to get the second tier priorities. The information hasn't flowed quite to the extent we would like it to. Mr. Glen added that we are trying to extract that information from the design builder even when they are not ready for us to extract that information. Despite them not providing that information, we are tracking locations of early construction beyond the 7 or 8 that we have talked about in the past. We are looking at which ones have critical mass and with a considered effort can deliver ROW to start as with the 7 or 8 we have talked about. We intend to use this model and emulate it throughout all of the projects. This is a cooperative partnering with the design builder that allows us to get to the parcels they need to construct, recognizing we need to push the 1,400 parcels past the finish line simultaneously. Mr. Jarvis added that we have transitioned that with CP2-3 as well thru the RDP's GIS system. We have looked at where we have the parcels, the mapping and we are starting to work with the contractors as to where they can go to work based upon those massive parcels. Mr. Glen added that he did not mention in the report that we did certify the first CP4 parcels last week. The model is to try to get out ahead of it. Mr. Richards asked if there is anything in ROW that is causing a challenge to any of the design builders to go to Mr. Morales suggesting they can't meet requirements because the Authority has not delivered. Mr. Glen replied that we did get

ahead with CP2-3 and we continue to make good progress there. We continue to refine the ROW needs so there may be some recycling of those parcels. We do expect to have critical parcels in place to allow them to start early in 2016. We expect to do the same thing in CP4. With CP1 the concerning effort is with the partnering effort to identify the locations that are critical, to get those parcels delivered so they can start construction and follow up shortly after with the next wave of parcels that is needed to maintain construction activities at each of the sites. Mr. Richards asked in regards to capacity in terms of production on CP1 where are they. Have they reached some level at which they can't handle more construction? Mr. Jarvis replied that the critical path is primarily design approvals. Once they get design approvals, that often involves multiple third parties, you'll see additional construction done at more locations. ROW is not hindering their capacity. Mr. Richards asked how that is affecting the completion date that we contemplated with CP1. Mr. Morales replied that they are still contractually obligated to meet it. We have not finalized a mitigation schedule that we have to deal with what we know is an upfront delay. We have had discussions but we haven't gotten down to the formal steps it would take to erase that deficit that was created at the front. We have some ideas and we'll work thru them to see if they work from our perspective and from theirs. Mr. Richards asked when we think we'll have them resolved. Mr. Morales responded that he would estimate within this quarter. It's getting to that point of getting to the critical mass of ROW and to the critical mass of design approvals. To some extent for the contractor it's also a question of they don't want to deploy then stop then start again. The contract dates are what they are until we change them.

- Mr. Richards asked if on CP1 if we retain the exposure of AT&T, PG&E, the Railroads and the City of Fresno. Mr. Engstrom responded that is correct. Mr. Engstrom reported that 25 of 28 agreements on CP 2-3 are executed, and those that are not executed are tied to legal issues, CP 4 will be included next month. Mr. Richards asked Mr. Griggs for detailed information on cost estimates on AT&T, PG&E, Railroads and possibly the City of Fresno. This is a high priority for the information takeoffs, unit quantity and costs to the extent possible with best estimates at the time from an independent estimator. Mr. Engstrom stated that he received a recommendation from Mr. Griggs' group including what the contract value relative to the quantities are known today. Mr. Richards asked if this is in detail. Mr. Engstrom replied it's not in detail. Mr. Richards asked for Mr. Griggs to get Mr. Engstrom the additional information. Mr. Rossi stated that he assumes we already have it because probabilities have been run that couldn't be done without that data. Mr. Tapping replied that the Authority is running a risk overlay on the preliminary data, but that the ongoing risk analysis will be built on the additional updated cost estimate information to be provided to Mr. Engstrom. Mr. Richards added that we want to be sure of the information we have. Mr. Jarvis added that we are going thru a reconciliation process. The Project and Construction Management team (PCM) has established an estimate and a subconsultant of the RDP has established an estimate. There are a couple of key issues where they vary fairly significantly. Those two teams are getting together and going thru that process to reconcile the estimates. We do have the information but we don't have 100% confidence in it yet. We are working with our experts to reconcile their opinions. Mr. Griggs added that going forward we are going to use a different approach. The problem we are having is understanding what the scope of the utility work is. We need to do more investigation before we establish provisional sums. Mr. Rossi asked where this budget lies. Mr. Fong responded on the Capital Outlay Report. Mr. Rossi asked if it is separate from CP1. Mr. Fong replied yes. Mr. Morales added that it is not within the contract amount with the construction packages. It is a separate line item. Mr. Rossi asked if we can reconstruct the report to show this with the CP1 budget. Mr. Richards agreed that it is important to have a comprehensive all in cost for the first 29 miles that incorporates everything.
- **Executive Summary** – Mr. Rossi asked if at 20% vacancy that are hiring as quickly as we can. Mr. Morales responded that part of the reason for the vacancy is when a new position is added it is vacant and as we have hired we also have lost people. What we are losing primarily are traditional state jobs where people are looking for promotions and advancements and going to other departments. At one point we hired about 75 people with about 30 going to other places so we had to back fill. It's a constant

process and we may never get to 100%. We had initial delays which had to do with the engineering and technical support. We had to go out and get new classifications and develop tests. That is behind us now. We are continuing to hire those key positions and fill all others. Mr. Fong added that as of today we are at 16% vacancy. Mr. Richards asked if it is Ms. Harper's job to determine the number of positions we are asking for. Mr. Morales replied that it comes thru the budget process that is coordinated through the financial office because it results in a budget change proposal. We survey each division to see what they think they need in terms of additional bodies. Ms. Harper can look at whether we have flexibility to move bodies from one place to another. The primary focus is to get it out of the divisions at their request of what they need to do it. Then we roll it up together to the Department of Finance and thru the budget process. Mr. Fong added that it is always a balance between the vacancy rate and what you're asking for. Mr. Rossi asked how the vacancy rate and staff come together with consultant work. Mr. Fong replied that for his division he has not added any Authority staff since he has been here in 2 ½ years. A lot of that is he finding out where we are going to be and there are some skill sets that we do not have in state service. We rely a lot on consultants at this time. Mr. Morales added that one of the first tasks of the RDP was to develop jointly with the Authority a staffing plan which looked at a combination of state and consultant resources. We worked with each of the groups to determine what that balance is and where the gaps are needed to be filled. That feeds the budget process where we ask for state positions. We have a total look at combined resources of state employees and the RDP to fill out the functions. In the Financial Office we have financial advisers in that role. We have a consolidated look at what are total staffing is with the core team of state staff, RDP and KPMG. Mr. Rossi asked how do you decide that the staffing is correct and what is used as a reference. Mr. Griggs responded that we had alignment sessions where we meet together to see what resources we need. We have worked closely together at the hiring side to make sure weren't hiring the same position. Mr. Jarvis added that we develop an integrated functional org chart for each of our functions that need to be accomplished. We put the people that we have into the functions and then we can determine where are holes are. The first thing we do is look to fill the position with RDP. If it more appropriate to fill the position with state staff, at a very limited scale we move those requests thru the BCP process. Mr. Fong added they we also need to make sure the skill set is available thru state service and the position is temporary. What we don't want to do is staff the wrong positions and have permanent state staff.

Mr. Rossi asked for an update on risk analysis. Mr. Tapping replied that updated risk analyses are ongoing for CP1, CP2-3, and CP4. The CP1 ROW and adjacent railroad requirement cost risks were initially identified when the CP1 contingency was established; however, early indications are that these risks are trending negatively if not mitigated. Mr. Tapping stated that the Authority is assessing mitigation strategies for these and other risks and this will be addressed in the draft 2016 Business Plan, currently under development. Mr. Tapping also stated that Authority is currently assessing third party issues and providing a risk overlay for the estimates to establish confidence levels. The Authority is also working on a risk-informed contingency recommendation for CP4, expected to be presented at the March Board of Directors Meeting. Mr. Rossi identified that the CP 1 probabilities are trending towards exceeding the current approved contingency, but there is time to mitigate. Mr. Richards asked if Caltrans is our largest third party contract in CP1. Mr. Jarvis replied that it is not technically a third party agreement. We have a direct contract with Caltrans. Mr. Richards asked what type of exposure we have. Mr. Jarvis replied that we do have some exposure but it is hard to quantify. It a CMGC (Construction Manager General Contractor) contract and the guaranteed maximum price for construction has not yet been established. Mr. Richards asked what is the \$225.9 million? Mr. Jarvis replied that that was the estimated maximum cost to deliver the project for both the support costs, the ROW and the construction capital costs. Theoretically there could be exposure to pay more than that. At this point Caltrans is in negotiations with the contractor. With CMGC you hire them to provide design support then you negotiate for the construction costs. At this point we don't know where that will end up. Mr. Richards added that when asked about that previously it was stated that it was a fixed

price contract. Was the intention to say it will eventually be a fixed price contract? What we didn't hear is that it is not yet a fixed price contract. Mr. Jarvis added that what we are going to fix in is that guaranteed maximum price for the capital construction cost with a contingency and move forward from there. Mr. Rossi asked if it could be larger than the \$225.9 million. Mr. Jarvis replied yes. Mr. Richards asked how that hits the risk analysis. Mr. Tapping replied that the Authority will be performing a cost risk and sensitivity analysis around each party's estimate associated with the proposed CMGC fixed price. There is going to be some uncertainty around it. Mr. Richards asked how long with this take. Mr. Ogle replied that we are about 2 months away. We started getting the estimates back from the contractor. Then they go into negotiation to get the maximum fixed price. They have already gone thru the first negotiation with an early work package which started last month. Once we get that information that we will negotiate with that. Mr. Richards asked with the relationship with Caltrans, is the contractor required to submit 2 or 3 bids for each subtrade. Mr. Ogle replied yes. Mr. Jarvis added that the process requires 3 overall bids with 1 established by Caltrans, 1 established by a possible contractor, and 1 established by an independent estimator. Those 3 are used in negotiations to establish the guaranteed overall price. Mr. Rossi asked if today we have any idea what the amount is. Mr. Ogle replied that he knows it will be over \$225 million. Mr. Griggs added that we are still seeing very competitive bids. CP4 just came in and it seems to be a good bidding environment so it should pay off on this contract as well.

Agenda Item – Audits – Paula Rivera

- None.

Agenda Item – CP 1 and 2-3 Project Update

- None.

Agenda Item – CP 1 & 2-3 and SR-99 Project Update

- None.

-Current Issues

- No current issues.

Meeting adjourned at 9:25 am.